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BEFORE THE
DEPARTMENT OF TRANSPORTATION
WASHINGTON, D. C.

Joint Application of

Delta Airlines, Inc.
Swissair, Swiss Air TransportCompany, Ltd.
Sabena, S.A., Sabena Belgian World Airlines, and
Austrian Airlines, Osterreischische Luftverkehrs AG

for approval of and antitrust immunity for Alliance Agreements pursuant to 49 U.S.C. §§ 41308 and 41309

Docket OST-95-618 - 35

COMMENTS OF TRANS WORLD AIRLINES, INC.

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Docket OST-95-6 18

COMMENTS OF TRANS WORLD AIRLINES, INC.

By an application, dated September 8, 1995, Delta, Swissair, Sabena, and Austrian Airlines have requested antitrust immunity for a series of alliance agreements under which they will pool revenue, fix prices, limit capacity, and agree upon travel agent commissions in the major markets between the United States and Belgium, Switzerland, and Austria. The agreements would also allow the applicants to coordinate schedules in order to expand code sharing service between the United States and countries beyond the gateways of the European partners. The applicants have submitted only one of the agreements - a "Framework Agreement"(the "Agreement"), and do not plan to negotiate the other agreements until after antitrust immunity

has been granted. TWA hereby answers and requests that the application be denied. In support of its Answer, TWA states as follows.

At the outset TWA wants to state that it fully supports the Secretary's Statement of United States International Air Transportation Policy and his efforts to secure Open Skies agreements from other governments. TWA also supports alliances designed to secure competitive opportunities in international markets for U.S. flag carriers and benefits for consumers from enhanced service opportunities and competitive pricing. These agreements, however, go well beyond what was contemplated by the Policy Statement. They would limit competition between the U.S. and three European countries; they would limit competitive opportunities for other U.S. carriers; and they are not required in their proposed form to secure the benefits contemplated in the Policy Statement.

I. TWA'S INTEREST IN THIS PROCEEDING

It is important to understand why TWA is so concerned about this proceeding, even though it does not at present serve the three European countries of the alliance partners. TWA has both traditional competitive concerns as well as important strategic interests that would be affected by the grant of antitrust immunity to these carriers. In general, TWA believes that the proposed immunized Alliance will foreclose TWA's market opportunities both to the Alliance countries and beyond. In order to be an effective competitor, TWA needs an economically viable transatlantic system. To do so, it must re-enter routes on which it was forced to discontinue

service because of its financial difficulties and must find ways in which to expand the scope of its service to compete with the developing alliances. TWA believes that the proposed Delta alliances will have a chilling effect on its ability to compete.

TWA's first concern is that the alliance will foreclose TWA's potential re-entry into the alliance countries, TWA served Belgium, Austria and Switzerland for many years, and even had a code share agreement with Austrian Airlines. Its financial problems in the early 1990's, compounded by the impact of the Delta code shares with Swissair and Austrian without antitrust immunity, forced its withdrawal from these markets'. However, with TWA's re-invigorization, it looks forward over the next few years to returning to the transatlantic markets from which it withdrew, If Delta and the national carriers were independent competitors in each of these markets, TWA believes that it could reestablish a competitive position. Re-entry will be more difficult with Delta as the code-share partner of the national carriers. However, return to these markets would be impossible if Delta and its partners are actually operating as a cartel, combining their market power to compete with new entrants. The Delta proposal, if approved, would damage the competitive process.

TWA also competes with the alliance carriers in several beyond markets, including Israel, Greece, and the Middle East. While it believes that code share agreements in general provide a competitive advantage to its foreign flag competitors, that is not the issue in this case. Here, we

[1] Delta implemented code share agreements with Swissair and Sabena in 1993 and with Austrian in the summer of 1994. TWA discontinued its service to Brussels on May 1, 1994, to Geneva and Zurich on September 6, 1994, and to Vienna on January 8, 1995.

are concerned about the added competition that the applicants allege they will provide solely because they will receive immunity from the antitrust laws. TWA is willing to compete on an equal playing field with these carriers, even when they are code sharing. It does not believe that it should be handicapped by giving its competitors immunity from the antitrust laws.

Finally, TWA is concerned about the transatlantic hegemony that will be created by Delta with its multiple code share agreements enhanced by antitrust immunity. As discussed below, Delta does not need three duplicative immunized code share agreements to provide enhanced online service to particular beyond gateway destinations. There are only limited time channels for transatlantic operation, and Delta can meet the needs of its passengers with one code share connection as well as with three in the same time channel Delta's overkill strategy appears to be designed to preempt potential code share competitors, as much as to meet needs for consumer choice. Code share agreements come and go. However, code share alliances locked in place by antitrust immunity will be unlikely to ever dissolve, giving Delta a permanent competitive advantage over other U.S. carriers.

II. THE RETURN OF THE CARTEL

Before reviewing the details of the agreements, it is useful to place them in the context of the development of international aviation over the last three decades. Twenty five years ago, international aviation was characterized by limited competition, high prices, and pervasive inter - carrier agreements affecting all aspects of airline operations. Under the IATA system, which had

received antitrust immunity in the 1940's, carriers fixed the prices and conditions of service of air transportation, and established uniform travel agent commission rates. Bilateral agreements carefully limited capacity of national carriers on major routes, and the carriers themselves quite often agreed on the details of their schedules and the pooling of revenue earned on their flights. While revenue pooling was never accepted by the United States, on other major routes, carriers agreed upon formulas under which they would divide the total revenue earned by both carriers on the route. Since it did not make any difference which carrier actually transported the passenger, they did not engage in service competition.

This system began to break down in the late 1970's when the impact of American deregulation was felt in the international marketplace. Revenue pooling was sharply restricted by the European Community's First Aviation Package in 1987, and ultimately eliminated in 1991[2]. The United States removed immunity from the IATA agreements establishing uniform travel agent commissions in 1978, and from the domestic agreements in June 1980[3]. The IATA traffic conferences, which fixed prices, continue in existence, but are substantially weakened. The United States has conducted an extensive investigation of the conferences but has not yet determined whether to revoke antitrust immunity (Docket 46298). The conferences still negotiate fares, but carriers are not required to adhere to the agreements. Many major airlines, including TWA, are no longer members of the traffic conferences.

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[2] Coopers & Lybrand, EC Commentaries, August 3 1, 1995, Sec. 9.9

[3] IATA Uniform Commission Rates, 71 CAB 155 1 (Order 78-8-87); Competition for Agency Services Show Cause Proceeding, Orders 79-9-65, 80-2-33, 80-5-159.

The applicants propose to reestablish the cozy cartel that existed prior to deregulation. While they emphasize the consumer benefits that would be provided through code sharing and coordinated schedules in beyond markets, the heart of the Agreement (Section 2.2) provides that they would jointly establish fares, control inventory, coordinate schedules and capacity, establish procedures for sharing or pooling of revenue in particular markets, and create a unified commission schedule for payment of standard and override commissions. In the cartel, the largest US transatlantic carrier, and three major national European airlines have agreed to restrain competition between the US and their homelands. Swissair, Sabena, and Austrian have combined with Delta to return to the 1970's.

III. THE APPLICANTS CANNOT RELY ON THE PRECEDENT OF NORTHWEST/KLM TO SUPPORT THEIR REQUEST FOR IMMUNITY.

The applicants have structured their case to be as similar as possible to that presented to Northwest and KLM, to whom the Department granted antitrust immunity in January 1993 Thus, they claim as follows:

> *The proposed networks and their proposed operations would be similar to those of Northwest and KLM (p.2)

> *The open skies agreements of Switzerland, Belgium, and Australia provide the same basis for grant of immunity as the Netherlands agreement (p.8)

> -There are no significant commercial competitive or aeropolitical distinctions between the proposed Agreements and the Northwest/KLM agreement that would justify denial of immunity (p.9)

•The proposed Agreements should be considered under the same "quasi-merger" standards as NorthwestKLM.

None of these claims are correct. Before reviewing them, it would be helpful to recall the details of the Northwest/KLM transaction as outlined in the Department's Orders approving the agreement (Orders 92- 1 l-27, 93- 1- 11).

A. Northwest/KLM had less market impact.

The NorthwestKLM alliance was much smaller than that of the applicants, and competed in fewer markets. Before the Northwest/KLM alliance was established in 1991, Northwest did not serve Amsterdam[4]. At the time of the application for immunity, the carriers competed on only two routes -- Detroit and Minneapolis/St. Paul-Amsterdam, where KLM operated the airplanes, and Northwest purchased 144 seats on each aircraft pursuant to a blocked space agreement (Order 92-l l-37, p.32). However service was limited to only 10 flights per week. Northwest also served Amsterdam from its Boston hub.

Northwest/KLM accounted for only 8% of total US-Europe seats, making them the 8th and 9th largest carriers. Even combined, they would have been the 5th largest carrier (Order 92-1 l-37, p.32).

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[4] GAO/RCED-95-99, International Airline Code Sharing, p. 16 (hereinafter, GAO Report).

In contrast, Delta is already the largest carrier on the North Atlantic, with 15.64% of total weekly frequencies (Application, Ex. 3). Combined, the applicants will offer 20.28% of all weekly services in the transatlantic market. Thus, the sheer mass of the proposed combination raises substantially more competitive concern than Northwest/KLM did.

B. Northwest and KLM proposed to operate as a merged carrier.

Another major distinction is that Northwest and KLM were proposing a truly integrated operation, under which the applicants would act almost as one carrier. At the time of the application, KLM had substantial equity interest in Northwest which it had acquired in 1989 (Order 92-1 I-27, p.2). Currently, KLM owns 2 1.5 % of Northwest's common stock.

As noted by Delta, the Integration Agreement between KLM and Northwest planned on the fundamental equivalent of a merger [5]. Section 1.1 of the integration agreement between KLM and Northwest provided that the carriers "hereby agree to integrate their commercial operation". In contrast, while the applicants state that "the alliance agreements are virtually identical to the Northwest/KLM agreement" (p.21), there is nothing of similar scope in the current Agreements. The Delta/Swissair Agreement, for example, provides only that Delta and Swissair "agree to enhance their commercial cooperation" through a series of agreements designed to achieve a high level of cooperation (Article 1.1). One of the telling differences between the current application and that of Northwest/KLM is that the Northwest/KLM agreement was titled a "Commercial

[5] Delta Petition for Reconsideration, February 4, 1993, p.2, Dockets 48342, 4637 1.

Cooperation and Integration Agreement", while the current Agreements are labelled only "Cooperation Agreement".

C. Foreign Expectations Are Not The Same In This Case As In Northwest/KLM

Applicants argue that foreign policy considerations support the proposed grant of immunity because the governments of the European national carriers will expect treatment similar to that of the Netherlands (pp.22-25). However, the Open Skies agreements with Austria, Belgium, and Switzerland are not the same as reached with the Netherlands and there can be no expectation by the involved governments that the current proposal would receive anti-trust immunity.

In the Netherlands agreement, the United States made an implicit promise that antitrust immunity would be granted. (Order 92-l l-27, pp. 21-22, 38). Thus, in the Memorandum of Consultations, the United States agreed to give "sympathetic consideration" to the concept of commercial cooperation and integration agreements and to requests for antitrust immunity between U.S. and Dutch air carriers. It is in the context of such "sympathetic consideration" that, in the language quoted by applicants, the Department found that it would be contrary to the spirit of the US-Netherlands agreement to deny antitrust immunity.

In this case, the US government has not promised "sympathetic consideration". Rather, it has only agreed in the Memorandum of Consultations that requests for immunity would "be given

due consideration on a case specific basis, taking into account US law and international policy at the time such request is filed"[6]. Obviously, this language is quite different from that of the US-Netherlands MOC. The United States has made no promise, expressed or implied, that it will grant antitrust immunity to these Agreements. Indeed, the other governments recognized that the antitrust immunity was not part of the Open Skies agreements, and that the US will not be obligated to grant it. The Belgian and Austrian MOCs stated that the belief of the European government that "antitrust immunity is an essential complement to Open Skies", a statement in which the US government did not join. Thus, the foreign policy situation here is quite different from that with the Netherlands, and does not require grant of antitrust immunity.

In summary, the approval under different circumstances by a previous Administration of the Northwest/KLM agreement does not bind the Department in this proceeding. This Administration has injected new vigor into antitrust enforcement, and has been more sensitive to the competitive impact of agreements in numerous industries. In Northwest/KLM, the two parties actually competed in only two city pairs, and the potential benefit in beyond markets far outweighed the limited effect of the agreement on existing competition. In this case, four major airlines, led by the largest transatlantic operator, will eliminate competition in ten city pairs. No beyond benefits can outweigh the detrimental effect of the proposed agreements on competition between the United States and three European countries.

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[6] Application, p.24: Emphasis added. The above language appears in the Belgian and Austrian MOCs. There is no discussion of antitrust immunity in the Swiss MOC.

IV. UNDER ANY APPLICABLE STANDARD, THE AGREEMENT SHOULD BE DISAPPROVED.

Under 49 U.S.C. §§ 41308 and 41309, the Department "cannot approve an intercarrier agreement that substantially reduces or eliminates competition unless the agreement is necessary to meet an important transportation need or secures important public benefits that cannot be secured by reasonably available alternative means having materially less anticompetitive effect" (Order 92-1 l-27, pp. 26-27). Under this standard , the Department must weigh the obvious reduction of competition in the gateway markets between the United States and three European countries against the consumer advantages of quasi-online service in beyond markets. The Department must also discount such alleged benefits to the extent that they could be provided without antitrust immunity, and balance the loss to competition on the transatlantic segments against the net gain in consumer welfare in beyond markets.

In Northwest/KIM, the Department applied this standard in a manner similar to that of the Clayton Act because the parties represented that they intended to operate as if they were a single carrier. Although the applicants suggest that they should be subject to the same test, the same principles do not apply. Rather, the Department must consider these the actions proposed under these Agreements as Section 1 Sherman Act violations created by independent companies, and weigh those violations against the alleged consumer benefit. To do otherwise would ignore the fundamental distinction between Section 1 and Section 2 of the Sherman Act. Because a single company can determine its own prices and capacity, it does not follow that four major

transatlantic airlines who have no intention to merge can do the same. In any event, even if treated as equivalent to a merger, the proposed Agreements would not pass the test because the applicant would not be allowed to merge under the Clayton Act.

A. The Merger Standard Used In KLM/Northwest Is Not Applicable Here.

In the Northwest/KLM case, the Department's antitrust analysis treated the transaction as if it were a merger because the parties represented that the agreement was intended to integrate the two carriers' operations so that they could operate as if they were a single carrier. The Department noted that:

> Northwest and KLM represent that the agreement is intended to integrate the two carrier's operations so that they will operate as a single carrier. The Agreement's intended effects accordingly are equivalent to a merger of the two carriers. In determining whether the proposed transaction would violate the antitrust laws, we will apply the standard Clayton Act test used in examining whether mergers will substantially reduce competition in any relevant market. Order 92-l l-27, p.29)

In this case, the merger standards do not apply because the applicants have no intention of operating as a singly entity, even if they could legally do so. Their application is very clever in claiming that the application should be judged as if it were a merger, but never affirming that, absent legal requirements, they would consider a merger. In their application, the alliance carriers carefully state "in order to gain these benefits, the applicants have decided to form an alliance

because **legal and other obstacles** preclude the formation of integrated route systems either individually or through mergers" (p.4). These other non-legal obstacles are not spelled out. However, for several reasons it seems clear that the applicants would not relinquish their separate identities to form a merged company, even if they could do so legally.

For example, Sabena has had a history over the past decade of substantial and on-going losses, coupled with significant labor problems under Belgian labor laws, It has remained afloat only because of state aid which has caused substantial controversy within the European Union, Swissair has recently acquired a controlling interest in Sabena in order to gain a foothold within the European Union. However, Sabena's labor problems are a liability and Sabena has indicated no interest in a full-fledged merger. Swissair acquired 49.5% of Sabena, with an option, exercisable after 2000, to acquire another 12.75%, if legally permissible'. Clearly, it has no intention of merging with Sabena, even after 2000.

Neither Austrian nor Swissair have given any indication of discarding their national identity. Indeed, the applicants candidly state that the purpose of the Agreement is to allow them to cooperate to the extent necessary to create a seamless air transport system "while retaining their separate corporate and national identities" (Application, p.2). Thus, in contrast to the KIM/Northwest case, it is inappropriate to consider the Agreements in this case only in the context of a potential merger between the applicants.

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[7] Airline Business, June, 1995, p. 13

B. The Agreements Substantially Reduce Competition Between the United States and Three European Countries.

In contrast to the limited competition in two secondary city pairs that existed between Northwest and KLM, Delta and the other alliance partners compete on ten nonstop transatlantic routes: five to Switzerland, four to Belgium, and one to Austria. These include:

City Pair	INS Traffic - 1994
New York-Brussels	270,846
New York - Geneva	182,764
New York-Zurich	284,653
New York-Vienna	139,465
Boston-Brussels	43,085
Washington-Geneva	N/A
Atlanta-Brussels	115,287
Atlanta-Zurich	144,725
Cincinnati-Zurich	44,868
Chicago-Brussels	158,238
Total	**1,383,931**

Source: Application, p.5; INS data

Although the service is via a blocked space code share, "each carrier prices and markets its own service and competes for traffic on the flights" (Application, p. 5).

The applicants attempt to minimize the amount of this competition by claiming that it "represents only a small portion of the carriers' total transatlantic services" (Application, p. 5). This is irrelevant because the markets are significant in themselves, no matter what portion of the applicants' operation they may encompass. In any event, the claim may be true for Delta, which is the largest carrier on the Atlantic, but it is invalid for the other carriers. Neither Sabena nor Austrian operate to any other point in the U.S. In addition to the Delta code share markets, Swissair operates only to Chicago and Los Angeles. Thus, for the European carriers, the immunized agreements will solve almost all of their competitive problems.

In only three of the above city pairs is there any nonstop competition. American operates nonstop between New York and Brussels and Zurich and from Chicago to Brussels. Connecting service by other carriers is circuitous and ineffective in these nonstop markets, particularly for business passengers (Application, Ex. 10).

In each of these markets, applicants propose to engage in activities that are anticompetitive by any traditional standard. According to Article 2.2 of their Agreements, they plan to agree upon:

1. The fares to be charged and the amount of inventory that will be allocated to each fare by each carrier.

2. Coordination of schedules - This apparently covers the nonstop sectors as well as creation of connecting hubs.

3. Pooling of revenue and sharing of profits in particular markets

4. The base and override commissions to be paid to travel agents.

These practices would be agreements in restraint of trade, and have been condemned for many years by the U.S. Government (see Section II, supra). There is no doubt that they would substantially reduce competition on routes between the United States and Belgium, Switzerland, and Austria. There is also no doubt that the ability to coordinate in the primary transatlantic markets is considered the primary benefit for the European partners. For example, Herbert Bammer, President of Austrian Airlines, explained his interest in immunity as follows:

> Code sharing alliances like Austrian's agreements with All Nippon Airways or South African Airways are good, he says. But antitrust immunity is better. ' I know there are passengers who don't fly with us but with Delta because it has a better price. Maybe we overestimate the transparency of each other's distribution system. We have information on how our people sell tickets. But I don't know how a travel agent in Braham, Minnesota sells it. That is why it is plausible to say that if allied airlines are not allowed to coordinate prices, they definitely have different prices in the market for the same product'*

TWA does not believe that the Department should sanction such transparent violations of the antitrust laws for the sake of vague and undefined benefits in connecting markets.

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[8] Austria: Psyched Up - Austrian Airlines Bounces Back, Airline Business, May 1, 1995, p. 66.

C. The Benefits of Improved Service to Beyond Countries Can Be Achieved by Reasonably Available Alternatives Having Materially Less Anticompetitive Effect.

1. Applicants Do Not Need Immunity to Provide Integrated Operations in Beyond Markets.

Under 49 U.S.C. §41309(c)(2), once others show that the agreements are anticompetitive, applicants have the burden of demonstrating that the public benefits of the agreement outweigh the anticompetitive effects. They have failed to meet this burden. The applicants allege that the major public benefits are the creation of significant service and pricing improvements through the expansion of online services made possible by the linking of their hub-and-spoke networks (Application, p. 2). At the outset, we should note that many of the applicants' generalizations about public benefits are so unreasonable and counter-intuitive that the Department cannot accept them without a hearing. These are detailed in Section VI, below. But even if the proposed creation of enhanced code share service to beyond points provides an important public benefit, it is clear that such service can be achieved by materially less anticompetitive means than granting antitrust immunity.

Numerous other code share alliances, both domestic and international, have achieved the same benefits without immunity from the antitrust laws. These alliances have coordinated schedules, established joint fares, and jointly promoted the code share service. The applicants

have not shown that they cannot accomplish the same results while complying with the competition laws of the United States.

1. **Through Fares -** The applicants propose to use the immunity to establish joint fares and share revenues on these routes. They complain that the joint fare process is tedious, and that they need immunity to use joint fare formulas (Application, p. 37). Such a claim is ludicrous in an age of computerization. Carriers are well able to handle hundreds of markets pursuant to a formula and have done so in both domestic and international transportation for many years, It is absolutely lawful, and indeed was required under the Federal Aviation Act, for carriers to establish joint fares for passengers moving beyond their route systems,

Moreover, the parties to a joint fare can create any prorate formula that they desire to share the revenue from a joint fare. They do not need immunity for one partner to provide the other an incentive through the prorate formula to route traffic. The added traffic achieved by both carriers normally provides an adequate inducement, but if that is inadequate, there is no antitrust violation in one carrier receiving a disproportionate share of the revenue. It is only in the gateway markets where the code share carriers are competitors that immunity is necessary to share revenue'.

[9] The Department of Justice agrees that "airlines need not engage in horizontal price fixing in order to interline effectively or efficiently" (Reply Comments of Department of Justice, Docket 46928, May 14, 1992, pp. 16-26).

2. Schedule Coordination - The carriers can also coordinate connecting schedules without immunity. Such coordination enhances competition by creating an alternative service for passengers, There is no doubt that domestic airlines and their commuter partners work together to create the most efficient connections at their hubs. It is equally clear that United and Lufthansa, and British Airways and USAir talk to each other about building connections. Such discussions may be difficult because moving one flight to create an international connection may break a connection in some other market. However, the parties can weigh the revenue potential of the alternatives, and make their decisions without immunity. Moreover, with blocked space agreements, the parties have had no difficulty in coordinating the direct schedules on which they block space from each other.

The applicants do not seem to have taken advantage of the code share rights they already possess. The open skies agreements have given each of the foreign flag partners unlimited access through code sharing to every domestic point Delta serves. Even without immunity, they can create coordinated scheduling with Delta in hundreds of markets. That they have not done so may be due more to lack of initiative rather than to fear of the antitrust laws.

The applicants suggest that immunity will allow them to coordinate connections over multiple hubs. Such arrangements are of little public benefit because of the limited time channels in which the duplicate connecting services would operate. The primary schedule times for transatlantic service are overnight eastbound, arriving in the morning, and midday westbound.

The ability of the applicants to offer alternative connecting points in the same time channel is of marginal public utility, and does not justify immunity.

3. Airport Coordination - Certainly, there is no antitrust problem in coordinating airport operations at a hub to provide a more seamless product for through passengers. Major carriers and their code share commuters do so at hubs all over the country, and international carriers share ticket counters, passenger lounges and other facilities, with or without code share operations, at points all over the world. Such coordination does not raise antitrust questions.

4. Joint Marketing - There is also no need for antitrust immunity to coordinate joint marketing activities at these non-gateway countries. For example, Delta could appoint one of its partners as its general sales agent in a country served on a code share basis, or all the alliance partners could appoint a joint sales **team** in such a country. Where the applicants are providing complementary service rather than engaging in direct competition, there can be no antitrust objection to joint promotion of their service.

2. The Applicants' Claims of Public Benefits are Unsubstantiated.

The applicants have made extensive claims about the purported benefits of their proposed alliance, which would flow only from the grant of antitrust immunity (Application, pp. 36-41). There is little dispute about the fact that the applicants can improve their financial results

private benefits.

by jointly setting fares and commissions, controlling the availability of discount seats[10] and eliminating "excess" capacity. What they have not demonstrated, however, is how these anticompetitive actions can be classified as a public benefit.

One benefit that indisputably would be a public benefit if it could be achieved would be a wider choice of frequencies and enhanced online services. The problem with the applicants' claim is that they simply assert, without any supporting evidence, that coordination and integration of schedules and route planning, not already possible through the code sharing and blocked space agreements, would result in that benefit. The assertion simply does not correspond with the realities of the marketplace and transatlantic scheduling.

Transatlantic schedules are constrained by the six hour time difference between the Eastern time zone of the United States and Central Europe and the need to efficiently utilize expensive intercontinental aircraft. Thus, as a practical matter --with or without alliances, transatlantic flights are scheduled to arrive in Europe in the early morning and depart in the late morning or at midday. Only in very large city pairs such as New York - London are flights scheduled outside of that basic time channel. Moreover, there is no evidence to support the contention that the European alliance carriers will adjust their schedules to provide greater choice of departure and arrival times for transatlantic passengers. In fact, current schedule practices suggest otherwise. The European carriers already have ample financial incentive to maximize

[10] The applicants' claim, at page 39, that the elimination of the competition inherent in existing blocked space agreements would increase discount seat availability simply defies basic logic and the concept of the role of competition in disciplining pricing in the market,

connections to their transatlantic services. Nevertheless, they do not, presumably because of other scheduling priorities, such as local market schedules and aircraft utilization. There is nothing in the application or in the information responses submited by the carriers to indicate that incentives will be changed.

The applicants would have us believe that the ability to coordinate pricing among four carriers actually is a public benefit. They claim that, in the absence of antitrust immunity, the need to engage in arms length negotiations effectively forecloses access to these behind-gateway city pairs, The sole support for this allegation is the GAO report, which in this instance relies on statements by representatives of Northwest and KLM--hardly disinterested observers. There is no evidence to suggest that the process of setting fares and dividing revenues among four carriers is any less cumbersome than arms length negotiations between two carriers. [11]

The applicants have quoted extensively from the GAO Report. They failed to call the Department's attention to the following language from the GAO's discussion of the Northwest/KLM alliance:

> DOT and Justice Department officials noted, however, that the high degree of integration that the two carriers have achieved would not violate antitrust laws if the carriers did not have immunity

[11] "The agreements available to other parties do not specifiy how revenues would be divided. However, since each member of the alliance is a separate entity, it must be assumed that any revenue division must address the individual financial interests of each carrier.

> because before the alliance the airlines were not significant competitors on most routes.
>
> (GAO Report, p.30)

TWA believes that the statement is also true of any integration of the applicants with respect to their proposals to provide enhanced service in connecting markets. The applicants differ from Northwest/KLM in the amount of their significant competition in gateway markets. It is for this that they need antitrust immunity, and not because of any benefits that they may provide in the form of enhanced service over their connecting hubs.

D. A Merger Among These Carriers Would Not Be Approved.

As we have shown above, it is inappropriate to consider the proposed alliance under the standards applicable to mergers because the applicants have no intention of merging even if it were legally permissible. However, even if the Clayton Act standards were applied to the Agreement, there is no basis for the grant of antitrust immunity. Under those standards, a merger would not be approved if it would substantially reduce competition in any relevant market (Order 92-l l-27, p.29). The proposed Agreement fails to meet this standard.

While the applicants argue that the only relevant market with which the Department should be concerned is U.S. - Europe, they have also provided argument with respect to national and city pair markets (Application, pp.25-35). Limitation to the U.S. -Europe market cannot be sustained. In Northwest/KLM, the Department found that there were three relevant markets:

U.S. - Europe, U.S. - Netherlands, and Detroit/Minneapolis-St. Paul-Amsterdam (Order 92-l 1-27, p. 32). The same policy should apply here.

U.S.-Belgium/Switzerland/Austria

The applicants do not argue that they will not have the dominant market share in the three national markets of U. S.-Belgium, U.S.- Switzerland, and U.S.-Austria. Rather, they claim that their market dominance should be of no concern for two reasons: (1) under the Open Skies agreements, any carrier can enter the nonstop market, and (2) ample onestop competition will discipline prices. Neither argument is valid. In fact, because of marketplace barriers, it would be difficult for any U.S. carrier to enter Austria and Switzerland in competition with the applicants, Moreover, connecting service of other carriers will not discipline the prices of non-stop service between the U.S. and these countries, particularly for business travel.

Open Skies - The applicants argue that they will not be able to raise prices above competitive levels because of the threat of potential competition. They claim "no U.S. airline will be foreclosed from serving any Alliance carriers' hub gateway cities, because there will be no legal impediments to their providing service".[12] However, the existence of an abstract legal right does not validate the claim that entry into these countries is easy as a matter of fact.

In effect, applicants are relying on the contestability theory used in the early days of deregulation, and long since discredited. For example, a recent economics textbook states:

[12] Response of applicants to DOT Information Item 5

> The theory of contestable markets (Baumol et al., 1982) argues that even in very concentrated markets, firms will not be able to hold the price above marginal cost -- will not have the power to control price -- if entry and exit are costless and can occur very rapidly. If these conditions are met, the force of potential competition alone will be sufficient to yield optimal market performance. This is, of course, essentially the same prediction that emerges from the static limit price model.
>
> The commercial airline industry was long touted as one of the markets most likely to meet the assumptions of the theory of contestable markets. Airplanes can easily be shifted from one route to another if profits make it attractive to do so. There are some problems with obtaining gates at major airports, but the point that assets are not sunk in particular routes seems valid enough. However, empirical studies have conclusively rejected the hypothesis that the airline industry is contestable. [Discussion of studies]
>
> ***
>
> No real world industry has as yet been shown to be contestable. The analysis of contestable markets has been a useful exercise to the extent that it has clarified the way market performance departs from the optimal in imperfectly contestable markets, It does not provide a tool that can be used to analyze the determinants of performance in real-world markets. [13]

In fact, while these markets may be contestable, there are significant barriers to entry. In particular, the national carriers exercise control over travel agents both through their CRS dominance, and through commissions and override payments. In Switzerland, where Swissair controls the national marketing company for Galileo, its CRS has an 80% market share[14]. While exact data is not available for Austria, the market structure is the same with Galileo, in which Austrian Airlines has an ownership interest, the predominant CRS. Only in Belgium is CRS competition relatively open, with the national carrier's CRS having a market share of only 37%.[15]

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[13] Martin, Industrial Economics: Economic Analysis and Public Policy, Second Edition, 1994, pp. 223 -224.

[14] SH&E, Study on CRS Charging Principles for European Commission, August 1995, p. 15.

[15] Ibid

In addition, the control of the national carrier over travel agents through payment or withholding of override commissions is quite significant. Because the national carrier generally carries at least 50% of all the traffic out of a country, substantially more than any individual competitor, travel agents earn substantially more in overrides by booking on the national airline. Conversely, if they fail to reach the goals established by the national carrier for payment of the override, they are severely damaged.

The proposed antitrust immunity would allow the carriers to establish override goals based upon booking of all members of the cartel. For example, Swissair may now pay a transatlantic override on an assumption that it will carry 50% of all translantic traffic out of its country. It may require agents to book half of all passengers on Swissair in order to run the override. However with the alliance, it can establish a goal requiring the agent to book 80 or 90% of all passengers on the alliance carrier. Thus, the alliance will substantially raise the barriers to entry into these markets.

A final barrier to entry will be the connecting hubs that applicants propose to create with antitrust immunity. In the United States, the applicants will have online connections through each Delta hub, equal to the connections available to any U.S. flag new entrant. At the European end of the route, the foreign carrier will also have a major connecting hub that the new entrant will be unable to match. The applicants' responses to the Department's information requests demonstrate that significant competitive entry is not a realistic expectation. At each of the European hubs at issue, a significant portion of the traffic carried on transatlantic service is Sixth

Freedom traffic, originating and or destined to points behind the gateway. In order to capture that traffic, the new entrant would have to establish a connecting hub at the European gateway -- a clearly impossible task. Even if the new entrant could obtain Fifth Freedom traffic rights to behind-gateway points, establishment of such a hub would be precluded by the lack of sufficient takeoff and landing slots".

Connecting Service - Applicants also argue that the availability of connecting service over other European gateways will eliminate the ability of applicants to raise prices above competitive levels or reduce the quality of service below that expected in a competitive market. Applicants exaggerate the impact of inferior connecting service, when compared to the nonstop operations of the alliance carriers. This is particularly true with respect to business passengers, who fill the high yield business class cabins of the nonstop operators. The availability of connecting service may discipline prices for tourist traffic, but will not do so for business class fares. Business passengers simply will not take routings that are 125-l 50% longer than the nonstop service.

Individual City Pairs - Antitrust immunity would also reduce competition in the ten city pairs in which the alliance carriers provide code share service. Only three of those city pairs have competitive nonstop service, and even in those markets, the competitive service provides substantially less than half of the capacity. For example, in both the New York-Brussels and New

[16] At Zurich, Brussels, and Vienna, slot availability during the peak morning hours for transatlantic service is limited. See responses to the Department's information requests,

York-Zurich markets, American provides nonstop service, but operates only a B-767, compared to a B-747 by the code share carriers. In Chicago-Brussels, the alliance carriers operate a DC-10, compared to a B-767 for American.

The availability of connecting service in these markets will have the same limited impact as in national markets. The alliance carriers may remain competitive for coach discount traffic, but they will not be inhibited in raising business class fares.

Thus, even under the Clayton Act standard proposed by applicants, the alliance Agreements must be denied immunity.

V. GRANTING OF ANTITRUST IMMUNITY TO THE ACTIVITIES OF THE ALLIANCE IS PREMATURE

The Agreements submitted by the applicants do not in themselves establish the arrangements under which the carriers will cooperate in marketing air transportation. For example, the Delta/Swissair Agreement states that its objective is to "to establish a legal framework" under which the carriers may expand the current cooperative agreements, and to "set forth the principles governing the development of additional agreements" (Articles 1.2, 1.2.2). The applicants admit that "the alliance has not yet been formed, however, and its route structure and service plans have yet to be established" and that they "have not reached agreements regarding service and equipment changes that would result from the alliance" (Responses to DOT

information items No. 5 and 10). Thus, the current agreements before the Department are merely "agreements to agree". They do not, therefore, justify grant of immunity for the underlying activities that would be agreed upon in the next round of discussions between the carriers. At most, the Department should grant discussion immunity, and require the carriers to submit their actual operating agreements for public comment and detailed review. Only then should the Department consider grant of full immunity to the Agreements.

VI. A HEARING IS NECESSARY TO EXPLORE THE APPLICANT'S COUNTERINTUITIVE AND CONTRADICTORY CLAIMS.

The Applicants' claims of public benefit are either unsubstantiated assertions, illogical, or both. TWA believes that a hearing is necessary to determine the validity of their statement and the real impact of antitrust immunity. The Department should require the Applicants to substantiate those claims and should give other parties the ability to critically examine and rebut them.

For example:

- The parties would coordinate pricing and inventory control (Application p. 12), an anticompetitive action, but claim that the result will be expansion of discount fares and discount seat availability (p.39). A further claim (p.40), both unsubstantiated and contrary to the workings of the competitive marketplace, is that cost reductions from coordinated inventory control would be passed on to the traveling public. The Department must recognize that there are now so many price categories that real pricing action occurs in the

control of inventory. With common inventory control, the Alliance carriers will eliminate any vestige of price competition. The Department cannot understand how the applicants system will work without a hearing.

- They claim that, while deep discount fares are now available only on each carrier's system, antitrust immunity would permit them to expand those fares to connecting service operated by the alliance carriers. The applicants do not explain why, if it is in their financial interest to offer such fares, they do not do so now on a joint fare basis.

- Presently, through their blocked space agreements, Delta and its code share partners are competitors. Under the Agreement, that competition would disappear. Yet the applicants would have us believe that the result would be greater discount seat availability because the parties would seek to maximize the efficient use of the seats offered. They do not explain how, with less competition, efficient use equates to greater availability of low fares.

- The applicants claim that antitrust immunity is required to establish prices and proration of revenue in behind-gateway markets. Relying on the GAO Report, p.29, they assert that without immunity establishment of joint fares and revenue prorates requires arms length negotiations that are too cumbersome to be practical. They do not explain how the negotiation of revenue division among four carriers would be less cumbersome than bilateral negotiations.

- The Applicants claim that antitrust immunity would enable them to operate transatlantic services that otherwise would not be economically feasible. Each carrier already has an economic incentive to maximize transatlantic connections at its hub and to capitalize on service opportunities. In fact, three of the applicants have already launched Washington, D.C. - Geneva - Vienna service without any need for antitrust immunity. The applicants fail to identify how an immunized alliance would create additional economic incentives,

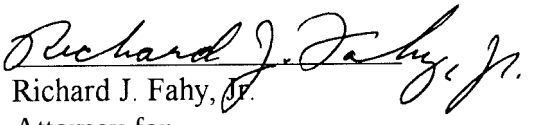
- In asserting that a combination of four carriers, with multiple European hubs serving many of the same behind-gateway markets, is in the public interest, the Joint Application relies extensively on the KLM/Northwest alliance, which involves only one European carrier and only one European hub, Amsterdam. The Applicants have submitted no evidence about the incremental benefits provided by the third and fourth members of the alliance, as compared to their effect on competition.

- The Department must determine if the public benefits claimed by the Applicants require an alliance between Delta and three European carriers or whether there is a less anticompetitive means available.

WHEREFORE, TWA respectfully requests that the application of Delta, Swissair, Sabena, and Austrian Airlines for antitrust immunity for their alliance Agreement be denied. At most only discussion immunity should be granted, and the Department should require submission of the

further agreements for review before considering grant of immunity to the operating agreements reached by the applicants.

Respectfully submitted,



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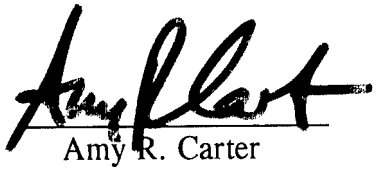
November 13, 1995

CERTIFICATE OF SERVICE

I hereby certify that I have on this day served a copy of the foregoing Comments of Trans World Airlines, Inc., upon all persons named on the attached service list via first class mail, postage prepaid.



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